OFFICE OF AUDITS
MEMORANDUM REPORT 97-CI-013
U.S. MISSION TO THE UNITED NATIONS
HOUSING PROGRAM
JUNE 1997

In accordance with the Office of Inspector General's (OIG) FY 1996 audit plan and as required by Public Law 100-459, section 9 (22 U.S.C. 287e-1), we reviewed the United States Mission to the United Nation's (USUN) housing program. The legislation requires the OIG to review the program periodically; our last review was performed in 1991. In FY 1996, the Department spent $984,000 to support the housing program. USUN, the Bureau of International Organization Affairs (IO), and the Bureau of Finance and Management Policy (FMP) manage the program.

The objectives of this review were to determine whether the (1) program complies with the authorizing legislation, and (2) required employee contributions are accurately computed and collected. While our review determined that USUN and IO are generally managing the program in accordance with regulations, FMP is not following established procedures concerning employee contributions (see pages 8-10). At the conclusion of our field work we identified $33,593 owed and an additional $74,955 potentially owed (a total of $108,548) to the Department by present and former USUN employees. We made recommendations to address the weaknesses identified in the housing program's financial management.

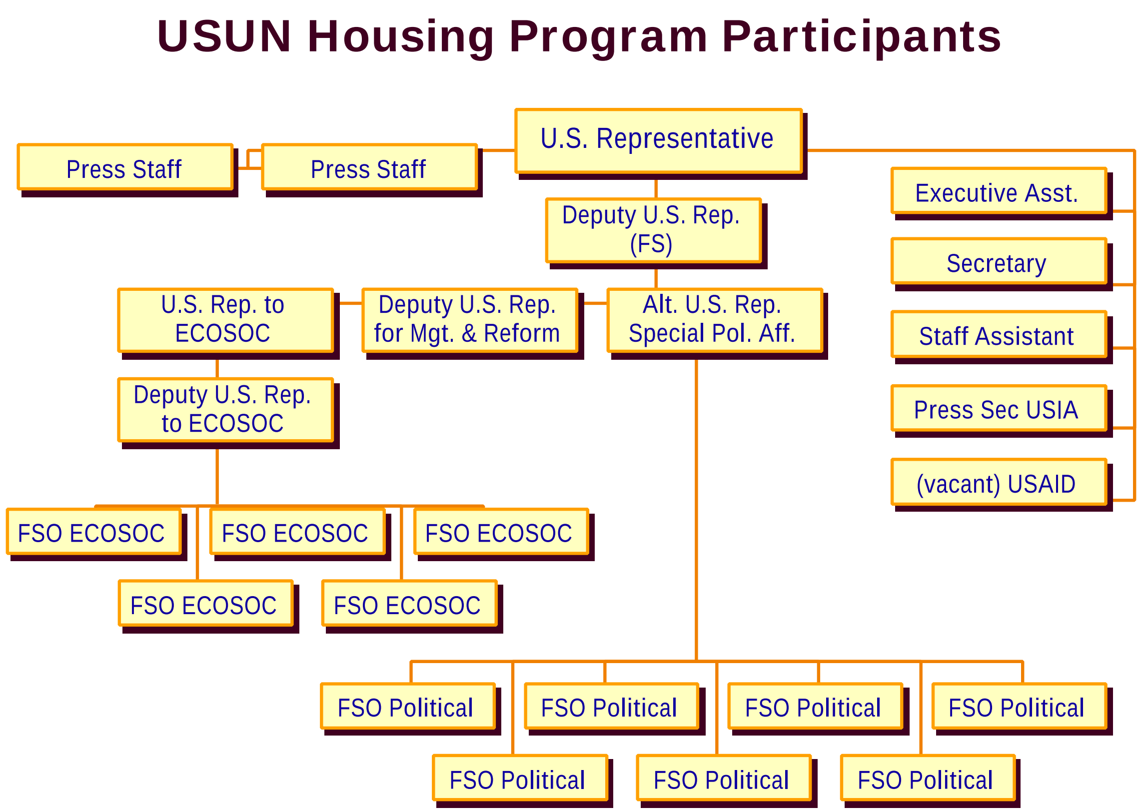
SCOPE OF REVIEW

To accomplish our review objectives, OIG performed field work at USUN in April 1996. Audit work was also performed at IO and FMP from March to June 1996. At all locations, OIG met with program officials and reviewed relevant documentation. At FMP, we analyzed housing program financial records for 1993 and 1994 because these were the most up-to-date records that FMP had completed processing at the time of our review. We also administered a questionnaire to housing program participants to obtain information concerning employees' views about the program and briefed USUN, IO, and FMP regarding the results of our review.

The review was conducted by the Consular and International Programs Division of the Office of Audits from April through June 1996, in accordance with generally accepted government auditing standards. Major contributors were Maurice Blais, division director; David Wise, audit manager; Irene Clark, auditor-in-charge; and Sharon Moorefield, auditor.

BACKGROUND

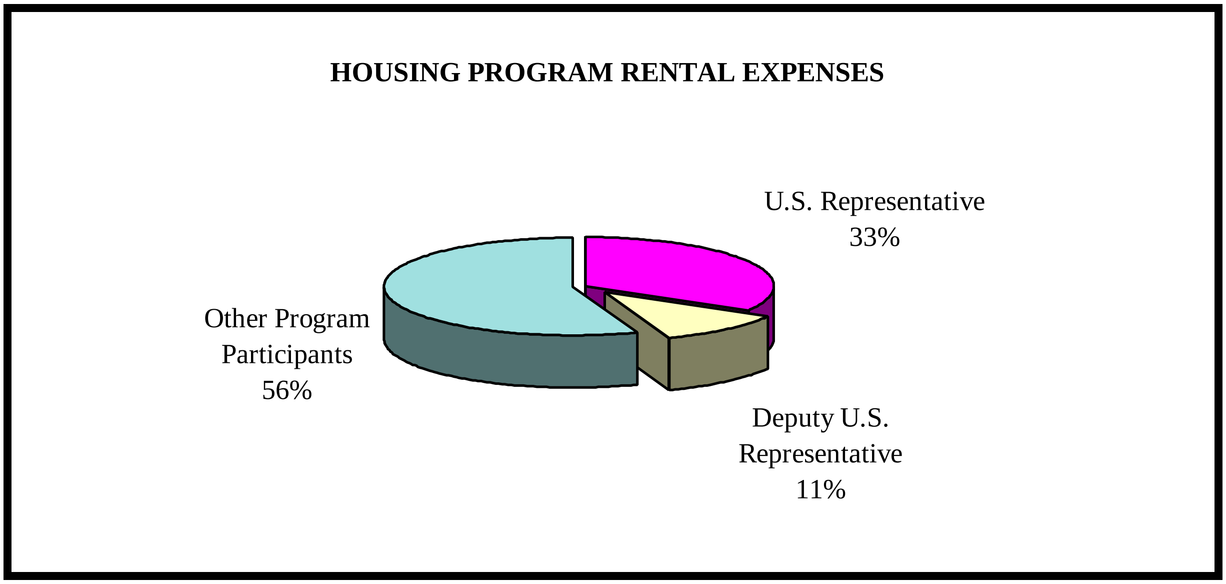
The high housing cost in New York City has traditionally been a strong disincentive for Foreign Service employees to accept USUN assignments. The main purpose of the USUN housing program is to compensate for the high cost of housing in New York City in order that the USUN may attract well qualified Foreign Service officers to apply for positions at USUN. The USUN housing program provides leased living quarters for up to 25 employees. These include the U. S. Representative and Deputy Representative to the United Nations, 18 foreign service employees of the mission, three other senior representatives, and two employees who serve at the pleasure of the Representative (Public Law 100-459, section 9 (22 U.S.C. 287e-1). The following diagram illustrates the housing program's participants:



FSO - Foreign Service Officer; ECOSOC - Economic Social; USIA - United Sates Information Agency; USAID - United States Agency for International Development.

<u>Housing Program Operation</u>

The Department paid $984,000 in rental benefits in fiscal year 1996, including $322,000 for the U.S. Representative's suite at the Waldorf Astoria Hotel, located six blocks from the USUN. The rent for this unit included maintenance, utilities, hotel security, and regular maid service. This amount represented nearly one-third of the total program. Excluding the residences of the U.S. Representative and Deputy Representative, the average rent per unit leased under the program was approximately $29,000. The following diagram illustrates how rental costs are proportioned among USUN housing program participants:



Except for the U.S. Representative and Deputy Representative, the cost of the lease is fully taxable to the program participants. Further, the program participants are required to contribute 20 percent of their base salary for payment into the housing program's appropriation account. However, the participants can offset their required 20 percent contribution by the amount of any Federal, State, and local income tax paid on the added rental benefits (Public Law 100-459, section 9 (22 U.S.C. 287e-1; and 2 FAM 049.6). This is called the "contribution offset."

The Department considers the USUN housing program a significant factor in attracting Foreign Service officers to apply for assignments at the USUN. This view was supported by the survey questionnaire we distributed to 19 housing participants. Of the 14 respondents, 10 indicated that they were generally satisfied with the program; 12 indicated that the housing program was a factor in their decision to work at the USUN.

Since OIG's first review in 1988, both the cost of the housing program operations and the number of housing participants decreased significantly. At that time, the cost of USUN housing program was about $2 million and provided housing for 44 USUN employees at an average cost of $47,000 per unit. Housing benefits for USUN employees were not treated as taxable income. In 1988, Congress mandated important changes to reduce housing program costs, effective July 1, 1989. For example, the number of eligible participants was reduced to the present number of 25 and the Internal Revenue Service (IRS) ruled that the housing costs paid by the Government are taxable as an employee benefit, except for the U.S. Representative and the Deputy U.S. Representative. Since then, the benefit has been considered as taxable income and the Department has reported the value of benefit (annual rent) to the IRS as additional income and increased the amount of tax withholding from the employees. Other changes included increasing employees' housing contribution from 5 percent to the 20 percent under the present arrangement.

Employee Contribution

The Department pays landlords on a monthly basis for leased apartments occupied by housing program participants. The rental benefit paid by the Department is included as additional income to the employee (except for the U.S. Representative and the Deputy U.S. Representative). To determine the amount of the employee's contribution, the annual rent is added to the participant's annual base salary. Tax is computed twice--first on the employee's total taxable income (from all sources including annual rent) to determine the total tax, then on the taxable income without annual rent. The difference between the two amounts is the tax attributable to the rental benefit. The tax on the annual rental benefit is compared to 20 percent of the employee's base pay. If 20 percent of the base pay is more than the tax attributable to the annual rent, the employee owes the Department the difference. If 20 percent is less than the tax on the annual rent, the employee does not owe the Department additional contributions. Although the added rental benefit increases the amount of their tax liability, this procedure generally results in program participants incurring modest or no additional expenses toward their rent after the final reconciliation. For example, in 1994, six of 28 participants did not owe the Department any additional contribution toward their rent after the reconciliation. The following example illustrates a case where the program participant was liable for $3,828 (9.7 percent) of the $39,491 rent paid by the Department:

PROGRAM PARTICIPANT TAX RECONCILIATION EXAMPLE

Annual rent		$ 39,491
Base Salary		100,856
Taxable income		$ 140,347
Tax per return	$ 44,395	
Tax without rental allowance	28,052	
Tax attributable to rent	$16,343	
20% of base Salary		20,171
Tax attributable to rent (-)		16,343
Due to the Department		$ 3,828

Program Management

Three Department entities are involved in managing the housing program--IO, USUN, and FMP; each has distinct duties and responsibilities.

IO provides broad oversight of the housing program, ensuring that USUN complies with program procedures. The bureau also disseminates information about the availability of positions as they occur and which positions are entitled to participate in the housing program.

USUN handles day-to-day management of the housing program. This includes (1) conducting market surveys to establish selection criteria, (2) setting maximum rents based on employee rank and family size, (3) reviewing all leases for adherence to the Department's worldwide space standards, (4) maintaining a detailed inventory of its housing units (including size in square feet, and number of rooms), and (5) reviewing/approving each housing lease before the Mission enters into the lease. USUN reports to FMP when an employee's participation in the program begins and ends. This report includes the amount of the participating employee's base salary and rental benefits.

FMP is responsible for administering employee contributions to the program and the subsequent income tax reconciliation. FMP's responsibilities also include billing, collecting, maintaining records on the amount of the employee contribution to the cost of their own housing, and ensuring proper income tax withholdings. An independent accounting firm, under contract with the Department, reconciles the 20 percent contribution with the tax attributable to the rent.

Prior Audits

Since 1988, OIG has issued four reports describing various problems in the program, including (1) excessive cost for leasing apartments, (2) the high annual rent for the U.S. Representative, (3) lack of a management plan, (4) lack of established procedures for collecting the required employee contribution, and (5) relocation expenses paid for the employees' convenience rather than for the benefit of the U.S. Government. OIG made numerous recommendations to address these problems. The Department has complied with the recommendations made in previous reports; however, this review found additional problems with the program's financial management.

RESULTS OF REVIEW

While IO and USUN have generally fulfilled their responsibilities in accordance with the regulations, FMP has not followed established procedures regarding employee contributions, and some former and present USUN employees have not paid their required contribution to the program and/or have not submitted the documentation required to reconcile their debt to the Department. At the conclusion of our field work, our analysis disclosed that the Department was owed $33,593, and potentially owed an additional $74,955, for a total of $108,548.

Financial Management

FMP is not managing the housing program billing and collection process in accordance with the established procedures. The Foreign Affairs Manual (2 FAM 049.7) requires FMP to ensure that the housing participants make their required contribution to the housing program and remit the money to the Department.

Housing regulations (2 FAM 049.7) state that program participants must submit relevant income tax information to an independent accounting firm within 30 days after the due date for filing the returns, for the tax reconciliation. A tax reconciliation is necessary for the employee to receive appropriate credit for the tax attributable to the rent. As a condition of participating in the housing program, each employee is requested to sign a statement agreeing to provide relevant tax information to the accounting firm. A contribution offset cannot be determined if tax information is not provided. Failure to provide relevant tax information could result in the employee paying the full 20 percent of the base salary. For example, one of the four participants who had been billed for the full 20 percent contribution for 1993 (discussed on page 9) subsequently submitted his tax return to the designated accounting firm in May 1996 and was allowed the contribution offset. In another example, a participant who did not submit a 1993 tax return to the accounting firm, paid the full 20 percent contribution in June 1996.

Our review disclosed that some USUN housing participants were not complying with the regulations. For example, in 1994, none of the 28 participants[1] submitted a tax return to the accounting firm on time. Late submissions delayed the tax reconciliation, billing, and collection process. When some participants were billed in previous years, they did not pay in a timely manner, and FMP subsequently allowed them to make installment payments. Delinquent payments by employees, in effect, resulted in interest-free loans from the Department. To avoid this situation, we believe that participants should be required to make their estimated rental contribution through biweekly payroll deductions.

The responsibilities of FMP and USUN employees with respect to USUN housing benefits are set forth in general in 2 FAM 049.7 and in greater detail in FMP's USUN Program Procedures. An FMP official stated these procedures were prepared in response to a 1990 OIG audit.[2] The procedures state that the Department's Consolidated American Payroll Division will render an interim bill to each employee in the housing program by December 31 of each year for the amount of required contributions to the housing program, or upon receiving notice from the USUN of an employee termination in the program, whichever is the earliest. The employee must pay the full amount of his/her required contribution 30 days after receiving the final bill, which will be sent approximately 30 days after the due date for submitting the Federal and other required tax returns to the accounting firm. No tax offset will be allowed if the employee fails to provide copies of the relevant pages of their Federal, State and local tax returns to the designated accounting firm.

> **<u>Recommendation 1</u>:** We recommend that the Bureau of Finance and Management Policy (FMP) notify each housing program participant in writing that each year's tax return is due to the designated accounting firm within 30 days of the due date for filing Federal tax returns (May 15 following the taxable year). If a filing extension is requested, the participant must provide FMP with a signed copy of any late filing forms sent to the Internal Revenue Service. FMP should immediately bill those who do not comply and should follow nonpayment by collection action to recover the full 20 percent of their base pay plus interest at the prevailing rate.

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[1] The housing program is allowed a maximum of 25 participants. In 1994, some participants started and others terminated over the course of the year.

[2] OIG's 1990 review of the housing program disclosed that housing regulations did not address how to determine the participant's contribution, establish payment dates, or identify how to remit the money to the Department. Without such procedures, participants did not know the amount of their financial obligations to the program or when to settle their debts.

Recommendation 2: We recommend that the U.S. Mission to the United Nations, in conjunction with the Bureau of Finance and Management Policy (FMP), implement procedures to ensure that housing program participants pay their required contributions, if any, through biweekly payroll deductions. USUN should retained this amount in the housing program's appropriations account. These procedures should also include a provision that if housing program participants do not provide the documentation required to determine their contributions, FMP will withhold 20 percent of the participant's base salary until such documentation is submitted. FMP should refund monies due to the participants after the accounting firm performs the appropriate tax reconciliations.

In its comments, FMP agreed with Recommendations 1 and 2 and included a draft proposal to revise the housing program including implementing an automatic payroll deduction and eliminating the need for lump sum payments by USUN employees. The FMP draft proposal appears to be an important step towards improving housing program management. Therefore, Recommendations 1 and 2 are resolved with the issuance of this report.

Criteria for Determining Employee Reconciliation

The USUN paid landlords $790,191 for 28 participants who rented apartments for either part or all of 1994. The designated accounting firm sends a report to FMP indicating the amount for which each participant is liable according to the following criteria:

- Participants who submit their tax returns to the accounting firm for reconciliation are liable for 20 percent of the base salary minus the taxes paid attributable to the lease value.

- Participants whose tax attributable to the lease value is greater than 20 percent of base salary owe no money to the Department.

- Participants who have not submitted tax returns to the accounting firm potentially owe the Department the full 20 percent of base salary.

As described in the following paragraphs, FMP did not fully adhere to the criteria for determining employee contributions.

Of the 28 participants in FY 1994, 23 submitted tax returns to the accounting firm for reconciliation but five did not. The accounting firm's reconciliations resulted in 17 participants owing the Department various amounts while 6 owed no additional contributions. As a result, in May 1996, FMP billed these 17 participants a total of $33,593. However, FMP did not bill the five participants who had not submitted their tax returns to the accounting firm. Accordingly, we calculated that 20 percent of the base salary for these five totaled $29,591. We also found that in FY 1993, four participants who did not submit returns to the accounting firm for reconciliation were eventually billed by FMP in May 1996 for $45,364 (20 percent of their base salary). The accounting firm reported the results of its reconciliation to FMP in a timely manner, but the bureau did not bill the participants within 30 days as required. As a result, the Department was neither reimbursed by those participants who owed $33,593 that was reconciled, nor by those who potentially owed $74,955 ($29,591 + $45,364) that was not reconciled--a total of $108,548.

FMP's May 1996 billings resulted from OIG's request to the bureau to provide a status of housing program financial liabilities. The following table summarizes the status of the financial liabilities of the housing program participants at the time of our review:

PARTICIPANTS' LIABILITY STATUS (1993 - 1994)

Year	Participants	Reconciled	Unreconciled	Totals
		Owed	Potentially Owed	
1994	17	$33,593		$39,593
1994	5		$29,591	$29,591
1993	4		$45,364	$45,364
Totals		**$33,593**	**$74,955**	**$108,548**

As a result of our review, FMP either collected full payment or is in the process of collecting through employee payroll deductions a total of $50,000 of the $108,548 for 1993 and 1994. Subsequent to our exit briefing in November 1996, the bureau also sent bills to participants who had not previously been billed and informed OIG that the bureau is still in the process of collecting the participants' liability to the Department.

Recommendation 3: We recommend that the Bureau of Finance and Management Policy send each participant a notice by December 31 indicating the amount that they are potentially liable for. The notice should state that any amount due must be paid by July 15 of the following year, or appropriate collection procedures will be initiated and interest will be charged at the prevailing rate.

FMP agreed with the recommendation. As noted on page 8 following Recommendations 1 and 2 , FMP has developed a draft plan to revise the housing program. Therefore, Recommendation 3 is resolved with the issuance of this report.

Recommendation 4: We recommend that the U.S. Mission to the United Nations provide all housing program participants an oral and written briefing that clearly states the employees' responsibilities. The briefing should ensure that participants understand the tax reconciliation procedures, their potential liability for the full 20 percent contribution, and instructions on how to calculate their estimated required contribution. All participants should acknowledge in writing that they have been briefed on their responsibilities and potential liabilities to the housing program.

USUN agreed with the recommendation and stated it would implement "at the earliest time." Therefore, Recommendation 4 is resolved with the issuance of this report.

Improper Reconciliation Procedures

FMP did not monitor the tax reconciliation procedures in accordance with housing regulations. The Foreign Affairs Manual (2 FAM 049.7) requires FMP to verify that housing participants are making the required contributions and determine if an additional amount is due to the Department. Housing regulations (2 FAM 049.6) state that the tax reconciliation should be based on only the participant's income and tax liability, and that each individual participant submit relevant tax information to the accounting firm. In some cases where the participant was married to someone not in the program and filing joint tax returns, the couple's combined tax liability was used to offset 20 percent of only the participant's base salary. As a result, the accounting firm used the (higher) combined taxable income from the tax return for the reconciliation. This procedure resulted in increasing the amount for the "tax offset" and lowering or eliminating the employee's contribution to the Department. Although we could not make a final determination based on the available documentation, we believe that additional money may be due to the Department because tax reconciliation procedures were improperly applied to married participants filing joint tax returns.

The following table illustrates how the combined tax of a participant and a spouse who was not a USUN employee was used to offset the base salary of a participant who worked part of a year. As shown in the following table, the tax per return was far greater than the participant's salary. While the data available did not prove conclusively that this individual would have owed the Department, it is clear that the existing procedures were not followed.

EXAMPLE OF INCORRECT TAX RECONCILIATION

Salary (with rent)			$48,275
Rent		17,771	
Base salary		30,504	
Tax per return	$95,120		
Tax without rental allowance	85,840		
Tax attributable to rent	$ 9,280		
20% of base Salary			6,101
Tax attributable to rent (-)			9,280
Due to the Department			$0

Recommendation 5: We recommend that the Bureau of Finance and Management Policy (FMP), in conjunction with the U.S. Mission to the United Nations (USUN), ensure that each participant who files a joint tax return with a spouse who is not a USUN employee understands the requirement to provide the accounting firm with only the participant's relevant tax information to enable FMP to verify the 20 percent contribution.

FMP and USUN agreed with the recommendation. As noted on page 8 following Recommendations 1 and 2, FMP developed a draft plan to revise the housing program. Therefore, Recommendation 5 is resolved with issuance of this report.

Cost of Housing for the Permanent Representative

The cost of housing for the U.S. Representative has averaged about $300,000 annually since 1991. In response to OIG's 1990 housing report, the Department's Office of the Procurement Executive performed a management study in 1991. The study included a cost benefit analysis of (1) buying, (2) building, and (3) leasing with option to buy other suitable lower cost housing for the U.S. Representative. The study concluded that while suitable lower cost housing could be found in the midtown Manhattan area, the additional costs that would be incurred for security, maintenance, utilities, and maid service would be substantial. The Representative is required to host many official functions, and frequently entertain high-level foreign and U.S. Government officials. The Waldorf Astoria Hotel where the Representative resides includes, among other benefits, a suitable room for entertaining at no additional cost.

Recommendation 6: We recommend that the Bureau of Administration, in conjunction with the U.S. Mission to the United Nations, develop a plan to review and analyze 1 year from the date of this report, and at least once every 5 years thereafter, the cost benefit of purchasing, building, leasing, or leasing with option to purchase a residence for the U.S. Representative. If the analysis favors one of the alternatives, the bureau should obtain the appropriate authorization and appropriate legislation that would enable the Department to buy, build, lease, or lease with option to buy a residence within the proposed limits.

The Bureau of Administration and USUN agreed with the recommendation. In its comments, the bureau noted that the responsibility for completing the task had been assigned to the Office of Real Property Management and that action would be completed on or before March 4, 1998. Therefore, Recommendation 6 is resolved with the issuance of this report.